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NECA NATIONAL EXCHANGE CARRIER ASSOCIATION INC

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July 27, 2000
Ms. Magalie Roman Salas, Secretary
Federal Communications Commission
The Portals
445 Twelfth Street, S.W.
Washington, D.C. 20554

Re: **Ex Parte Notice:** CC Docket No. 96-45, Federal-State Joint Board on Universal Service; CC Docket No. 99-294, Federal-State Joint Conference on Advanced Services

Dear Ms. Salas:

On Sunday, July 23, at the NARUC convention in Los Anageles, Bob Anderson, President, Ken Levy, Vice President and General Counsel, and I, all of NECA, Margot Humphrey, Esq., representing National Rural Telephone Association, Marie Guillory, Vice President, National Telephone Cooperative Association, and Bob De Broux of TDS met with Commissioners Nanette Thompson of Alaska, Bob Rowe of Montana, Bret Perlman of Texas and via telephone, with Laska Schoenfelder of South Dakota. A representative of SBC was also in attendance as an observer. We discussed the attached material, including the *NECA Rural Broadband Cost Study: Summary of Results.* The study estimates the investment dollars needed to upgrade rural study area lines in NECA's Common Line Pool to broadband capability at $10.9 billion. In light of this estimate, we discussed the need for universal service reform for rural carriers.

This filing is being made immediately upon my return to my D.C. office from the NARUC convention in Los Angeles. In accordance with Section 1.1206(a)(1) of the Commission's rules, two copies of this Notice are being submitted to your office for the above-referenced proceeding. Please address any questions to me.

Sincerely,

Enclosure
Cc: B. Perlman
R. Rowe
L. Schoenfelder
N. Thompson

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List A B C D E

High Cost Support
Embedded Cost Mechanism

Presented to: Rural Task Force

July 20-21, 2000 Seattle, Washington

OVERVIEW

- RURAL CARRIER HIGH COST SUPPORT
  - Continues to be based on relationship to National Average Cost per Loop (i.e., >115% of NACPL receives support)
    - Subject to certain limitations
  - Data collected and filed by NECA, program administered by USAC

Data Collection Process

- FCC Rules require all incumbent local exchange carriers to submit certain investment and expense data to NECA
  - non-rural carriers required to submit data quarterly
  - rural carriers required to submit data annually but may update data quarterly on a voluntary basis

- Data Collection Form included as Attachment A to presentation materials

Data Collection Process (cont.)

- Section 36.611 requires carriers to submit the following information:
  - Unseparated, state and interstate, gross plant investment in Exchange Line Cable and Wire Facilities (C&WF) Subcategory 1.3 and Exchange Line Central Office (CO) Circuit Equipment Category 4.13.
  - Unseparated accumulated depreciation and non-current deferred federal income taxes, attributable to Exchange Line C&WF Subcategory 1.3 investment, and Exchange Line CO Circuit Equipment Category 4.13 investment.

Data Collection Process (cont.)

- Unseparated depreciation expense attributable to Exchange Line C&WF Subcategory 1.3 investment, and Exchange Line CO Circuit Equipment Category 4.13 investment
- Unseparated maintenance expense attributable to Exchange Line C&WF Subcategory 1.3 investment and Exchange Line CO Circuit Equipment Category 4.13 investment.

Data Collection Process (cont.)

- Unseparated corporate operations expenses, operating taxes, and the benefits and rent portions of operating expenses. The amount for each category of expense listed shall be stated separately.
- Unseparated gross telecommunications plant investment.
- Unseparated accumulated depreciation and non-current deferred federal income taxes attributable to total unseparated telecommunications plant investment.
- Total and category 1.3 Working Loops

USF Algorithm

- With the data submitted, NECA utilizes an algorithm to develop individual study area and the national average loop cost.
- USF Algorithm included as Attachment B to presentation materials.

Expense Adjustment Calculation

- Any rural carrier (or non-rural carrier receiving hold-harmless support) whose study area cost per loop (SACPL) is greater than 115% of the national average cost per loop (NACPL) is eligible to receive high cost support, subject to the previously described limitations

Expense Adjustment Calculation(cont.)

- for study areas with 200,000 or fewer working loops, the expense adjustment (additional interstate expense allocation) is equal to the sum of
    - Sixty- five percent of the study area average unseparated loop cost per working loop in excess of 115 percent of the national average for this cost but not greater than 150 percent of the national average multiplied by the number of working loops for the study area, plus

Expense Adjustment Calculation(cont.)

- Seventy-five percent of the study area average unseparated loop cost per working loop excess of 150 percent of the national average multiplied by the number of working loops reported.

- 65% x costs between (115 and 150%) plus 75% of cost in excess of 150% of NACPL

Expense Adjustment Calculation(cont.)

- for study areas with 200,000 or more working loops, the expense adjustment (additional interstate expense allocation) is equal to the sum of
    - Ten percent of the study area average unseparated loop cost per working loop in excess of 115 percent of the national average but not greater than 160 percent of the national average multiplied by the number of working loops for the study area, plus

Expense Adjustment Calculation(cont.)

- Thirty percent of the study area average unseparated loop cost per working loop in excess of 160 percent of the national average but not greater than 200 percent of the national average multiplied by the number of working loops for the study area, plus
- Sixty percent of the study area average unseparated loop cost per working loop in excess of 200 percent of the national average but not greater than 250 percent of the national average multiplied by the number of working loops for the study area, plus

Expense Adjustment Calculation(cont.)

- Seventy- five percent of the study area average unseparated loop cost per working loop in excess of 250 percent of the national average multiplied by the number of working loops for the study area.

- 10% x costs between (115 and 160%) plus
  30% x costs between (160 and 200%) plus
  60% x costs between (200 and 250%) plus
  75% of cost in excess of 250% of NACPL

USF Limitations

- Currently three mechanisms in place that potentially place limits on individual study area loop costs and/or expense adjustment levels
  - Corporate Operations Expense Limitation
  - Cap on Growth in Total USF Expense Adjustment
  - Cap on Individual Study Area USF Payments

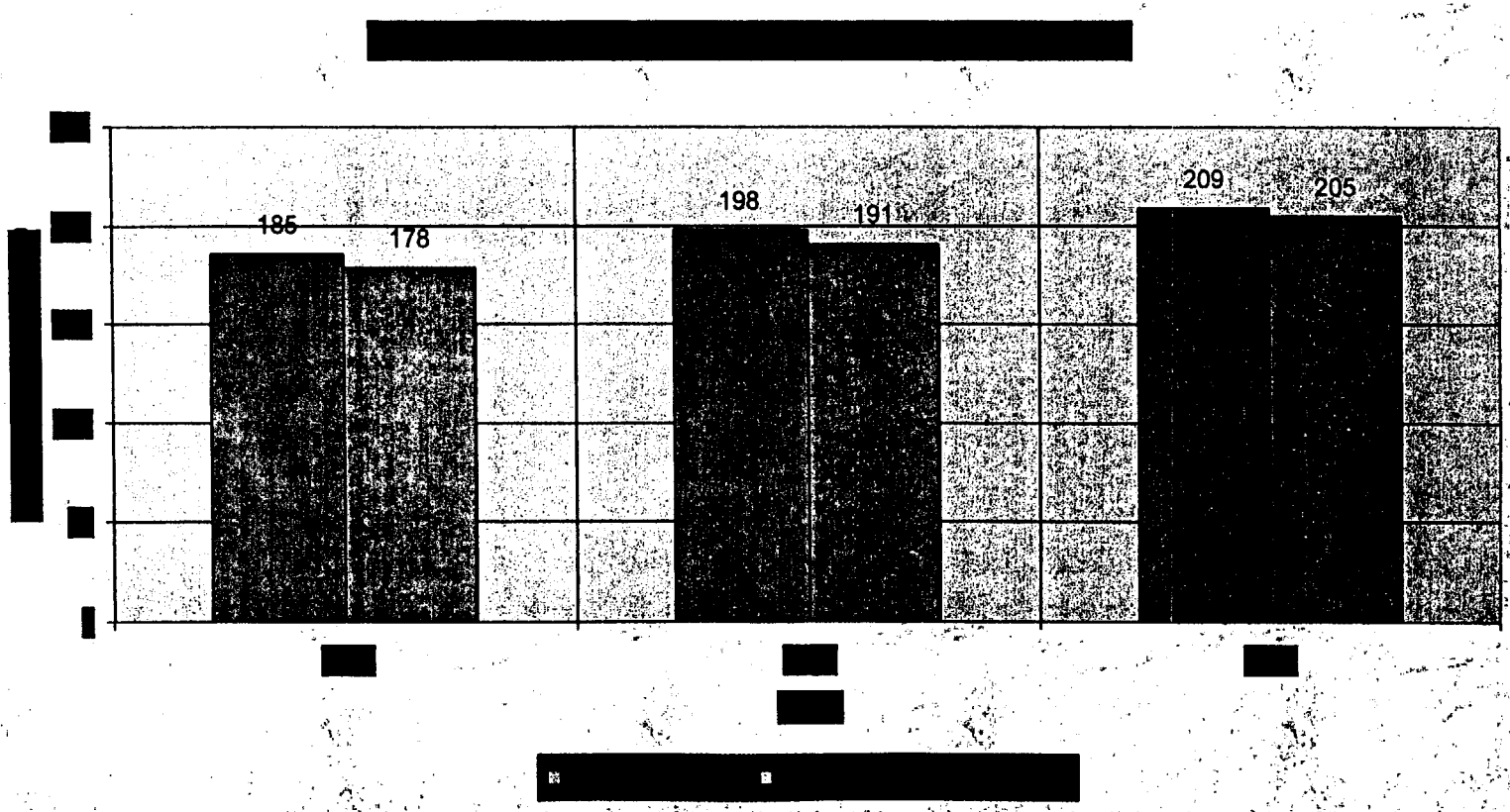
Corporate Operations Expense Limitation

- Since January 1, 1998 Total Corporate Operations Expense, for purposes of calculating universal service support payments, have been limited to the lesser of:
  - actual average monthly per-line Corporate Operations Expense; or

Corporate Operations Expense Limitation (cont.)

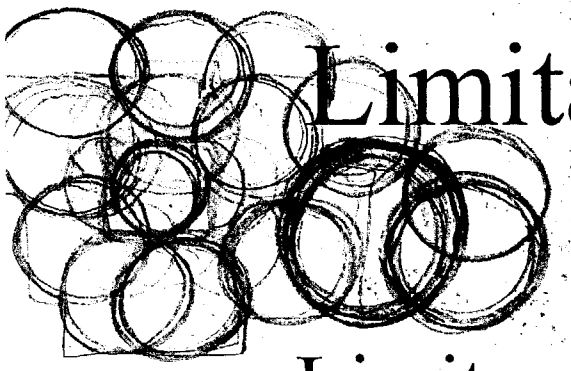
- For study areas with 6,000 or fewer working loops the amount per working loop shall be $31.188 - (.0023 x the number of working loops), or, $25,000 ÷ the number of working loops, whichever is greater
- For study areas with more than 6,000 but fewer than 18,006 working loops, the amount per working loop shall be $3.588 + (82,827.60 ÷ the number of working loops)
- For study areas with 18,006 or more working loops, the amount per working loop shall be $8.188

Corporate Operations Expense Limitation (cont.)



Corporate Operations Expense Limitation (cont.)

- Fixed $ per / loop limitation does not recognized inflation
- Number of rural companies impacted increasing annually
- Per company monthly impacts included in material at Attachment C



Limitation on Growth in Total USF

- Limit on Growth in Overall Fund Size introduced beginning with 1994 support payments.
  - The annual amount of the total nationwide loop cost expense adjustment calculated pursuant to Section 36 of the Commission's rules may not exceed the amount of the total loop cost expense adjustment for the preceding calendar year, increased by the rate of increase in the total number of working loops during the preceding calendar year.

Limitation on Growth in Total USF (cont.)

- Limitation accomplished through imputing a National Average Cost per Loop (NACPL) that produces the appropriate level of funding
  - calendar year 2000 "true NACPL" of $239.48 produced a funding requirement of $1,026M
  - imputed NACPL of $251.76 required to meet 2000 funding limit of $893.8M
- Support available for any study area whose annual loop costs are greater than $289.52 (115% of $251.76 or 121% of $239.48)

Impact of Limitation on Rural Carrier USF in 2000

- 133 Rural Study Areas lose all support due to higher threshold
- 1,019 Rural Study Areas monthly support reduced by up to $.92 per line

NECA RURAL BROADBAND Cost Study: SUMMARY OF RESULTS

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NECA Rural Broadband Cost Study: Summary of Results

Executive Summary

This study estimates the investment dollars needed to upgrade rural study area lines in NECA's Common Line pool[1] to broadband capability. Included in the estimate are plant upgrades on the customer side of the switch. Not included in the estimate are investment expenditures on DSL equipment, switch and backbone transport to other service areas or the ongoing maintenance of the upgraded network necessary to provide broadband services.

The results confirm two widely held beliefs about wiring rural America for broadband service[2] that seem contradictory on the surface. First, the estimated bill for completing the job is enormous, about $10.9 billion. Second, rural telephone companies are rapidly deploying a broadband capable network. According to the study's respondents, about 65% of rural lines will be capable[3] of providing broadband service by 2002. This fact, coupled with the ambitious rollout of data-network services documented in NECA's Access Market Survey[4], show that rural telephone companies are trying to meet their customers' needs for high-speed lines. Whether the pace is quick enough for policy-makers, or the targeted penetration rates are high enough for them to accept, will determine the funding needed to reach public policy objectives.

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[1] Based on the 1996 Telecommunications Act, the FCC has recognized 95 non-rural and 1301 rural LEC's (The latter includes both NECA and non-NECA companies.) Of the 1301 LEC's, 111 are companies NOT in the CL pool. A further investigation indicates that an additional 49 NECA LEC's were omitted from the FCC's rural/nonrural list. Therefore, a total of 1239 (1301-111+49) of NECA's CL pool members are Rural.

[2] The FCC defines broadband as "having the capability of supporting, in both the provider-to-consumer (downstream) and the consumer-to-provider (upstream) directions, a speed (in technical terms, 'bandwidth') in excess of 200 kilobits per second (kbps) in the last mile." Inquiry Concerning the Deployment of Advanced Telecommunications Capabilities, cc Docket No. 98-146, Report, 14FCCRcd 2398,2406(1999).

[3] A broadband capable line can potentially handle high-speed services. If the telephone company does not offer these services the line is still defined as broadband capable.

[4] National Exchange Carrier Association, Inc., Access Market Survey of NECA's Traffic Sensitive Pool Members - Keeping America Connected: The Broadband Challenge (1999)

Background

The FCC and several members of Congress have suggested the need for a targeted initiative aimed at deploying advanced telecommunications services in rural America. As defined by the Telecommunications Act of 1996 (Act), advanced telecommunications capability refers to "high speed, switched broadband telecommunications capability that enables users to originate and receive high quality voice, data, graphics, and video telecommunications using any technology."[5] A key concern is the ability to provide broadband capability in rural areas, where the cost of implementing necessary telephone network upgrades is expected to be significant.

There are a number of factors which typically increase the cost of serving customers in rural areas, such as large size of exchange areas, low line density, and scattered distribution of telephone customers. The exchanges of rural companies in NECA's Common Line pool cover 35% of the land area of the 48 contiguous states plus Hawaii, but serve just under 6% of 1990 households, or roughly 5% of 1998 USF loops.[6]

Report Highlights

The cost of upgrading rural local exchange carrier networks of NECA Common Line pool members was derived from two studies. The first was a detailed engineering study that was completed by a sample of companies that had or were in the process of upgrading their exchanges to broadband capability. This study measured the cost of upgrading lines. The second was a deployment study completed by a sample of other companies to estimate the percentage of lines that would not be upgraded to broadband capability by 2002.

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[5] Section 706 of the Pub.L. 104-104, Title VII, § 706, Feb. 8, 1996, 110 Stat. 153, reproduced in the notes under 47 USC § 157.

[6] Universal Service Fund (USF) 1999 Submission of 1998 Study Results by the National Exchange Carrier Association (Oct. 1, 1999).